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FINANCING THE HOME

ISSUED BY THE SMALL HOMES COUNCIL

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FINANCING THE HOME
SMALL HOMES COUNCIL AI.3

HOME OWNERSHIP

The builder or seller must be paid in full.

For most families, building or buying a house is the biggest investment of their lifetime; therefore, if you are thinking about home ownership and are typical of most prospective homeowners, you should give consideration to the many economic factors involved.

Since home ownership is a savings investment which entails some costs, you should know something about these costs. You should know how much you can spend for housing and whether you can afford to invest in a home. You should also know the business procedures involved in home financing. Unless you have some knowledge of these matters before you develop your plans to build or buy, you may encounter disappointments.

This circular presents general principles for financing a home. State laws and conditions vary so that some modification of the practices described on the following pages may be necessary in certain areas.

Financing Plan

Very few families have enough savings to pay for a home in a lump sum. Most of them have to borrow money to finance a home since the builder or the seller usually must be paid in full at the outset. They generally make a down payment from their savings and borrow the remainder.

The amount of down payment must be related 1) to the amount which can be borrowed, and 2) to the price of the house. The total amount available for a home, stated as a formula, is therefore:

Down payment	+	**Amount you can borrow**	=	**Total amount you can spend for a home.**
(Savings available for housing)		*(Based on your ability to repay)*		

In setting up your financing plan, you must:

- Determine how much money you can pay as a down payment. This will be your initial **equity** (share) in the property.

  The down payment usually will take most of your savings earmarked for housing. Certain preliminary and other costs involved in arranging the loan and securing the property will also have to be covered by this portion of your savings. (Be sure you retain enough savings to meet family emergencies, such as sickness and unemployment.)
- Find someone who, on your promise to repay, will lend you the balance of the money needed. To secure the loan, you will give the lender a **mortgage** on your property (conditional title to the property as a pledge of repayment).
- Set up a plan to repay the money which you borrow. This repayment must include not only the amount of money borrowed (**principal**), but also **interest** on the money — rent, so to speak, for the use of the money.

  Your repayment plan will be based on your housing budget allowance — or the share of your monthly income set aside for housing. This allowance will probably be used for regular monthly payments to pay the interest and to repay the loan. Taxes, insurance and upkeep can also be included in the monthly payments.

Costs of home ownership vary.

Acknowledgment

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WHAT CAN YOU PAY FOR HOUSING?

No formula can be established for determining how much a family can spend for a home. A practical estimate, however, can be reached by studying the family income and living expenses.

Housing is one of the largest items in the family budget.

Budget Allowance for Housing

Housing is one of the largest items in the family budget. For most families, it will take from 20 to 30 per cent of the income, either in rent or in ownership.

Low-income groups must spend a large part of their budgets for housing, food and clothing. As the annual income goes up, the family has greater freedom to choose the amounts to be spent for such things as housing, cars and recreation, or to be kept as savings.

A rule of thumb sometimes used to determine the amount to be spent for a home is: "You can afford a home equal to 2½ times your gross annual income." This would require 20 to 25 per cent of the take-home pay and is only an estimate since there are many modifying factors. Some families successfully finance homes worth three or more times their annual income.

Modifying Factors

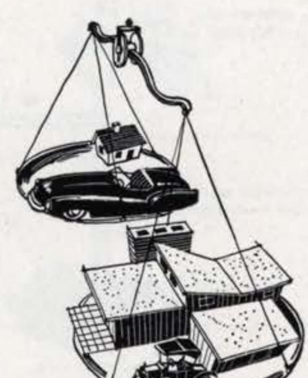
Your budget allowance for housing may be modified by certain factors:

- Two families having the same income may allot entirely different amounts for a home. Factors, such as stable employment or large savings for the down payment, might enable a family with an annual income of $4,000 to spend $10,000 to $12,000 for a home. Another family having the same income might spend more for a car or for vacations and entertainment, leaving less income for home ownership.
- A family with a number of children has greater requirements for food, clothing and medical care, and often will have less income remaining for home ownership than a smaller family. Sometimes, however, large families make greater use of the home for recreation, and can therefore budget more for housing than can a small family which is "never at home."
- Some people can reduce maintenance costs by doing much of the work themselves. Their costs being less, they can finance a larger loan. Neglecting maintenance in order to stay within an over-optimistic budget is not wise economy since neglect usually results in greater costs later.

Budget for Housing

To estimate how much you can spend for home ownership — or for rent, for that matter — study your expenses and determine on the basis of a budget how much of your income is available for housing. Plan a family budget by filling in the blanks below. (The figures can either be on a monthly or yearly basis.)*

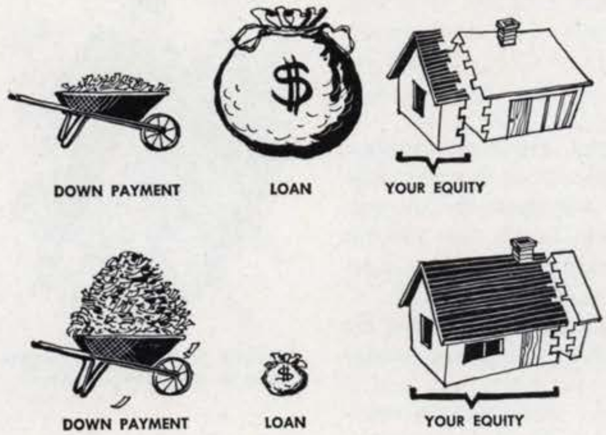
Food and Clothing	$______	**Total Income**	$______
Utilities and Fuel	______	Minus Income Tax and Retirement Benefits	______
Medical Care	______	**Total Net Income**	______
Life Insurance and Savings	______	Minus Total Living Expenses Other than Housing	______
Recreation	______	**INCOME AVAILABLE FOR HOUSING**	______
Transportation *(including car)*	______		
Installment Payments *(i.e., refrigerator, television set, washing machine)*	______		
Other Family Expenses	______		
Total Living Expenses Other Than Housing	______		



People with similar incomes spend varying amounts for houses and cars.

* If you want to put more income into your home, you probably can do so by cutting down on some other item in the family budget, such as recreational expenses. Do not, however, consider making major changes in your living standards.

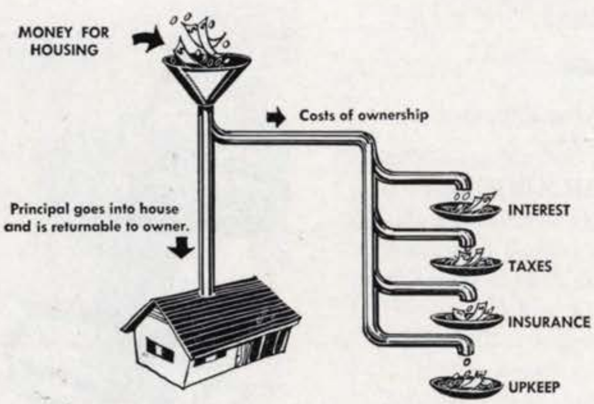
NECESSARY OUTLAY FOR HOME OWNERSHIP



The larger your down payment, the greater is your equity.

EXAMPLE

Amount of loan: $8,000		Interest rate: 5%
	15-year loan	*20-year loan*
Monthly payment	$63.27	$52.80
Total payment	$11,388.60	$12,672.00
Difference in monthly payments	=	$10.47
Difference in total payments (due to interest charges)	=	$1,283.40



Part of your outlay — that part which you pay toward the principal — is a savings investment. Instead of paying rent to others, you are paying it to yourself and investing it in property.

Expenses involved in home ownership and financing vary greatly. They depend on the rate of repayment of the loan and on interest rates, taxes, insurance, and maintenance costs. These expenses must be met when due.

Loan and Interest

Every cent of interest which you pay on borrowed money is an expense. The less you pay in interest, the better is your home ownership investment. You can reduce interest costs through:

- **A low interest rate.** Obtain the lowest rate possible on the basis of your record as a credit risk.
- **A large down payment.** The greater the down payment, the greater is your equity in the property and the less you will have to borrow. As a result, your total interest costs are less. Sometimes a large down payment also permits the lender to set a lower interest rate since the risk is reduced.
- **A short payment period.** The more you pay each month, the shorter period of time you will have to pay and, hence, the less total interest you will pay.
- **A loan which permits pre-payment** (payment in advance of the due date).

Because a long-term loan requires smaller monthly payments than a short-term one, it is usually best to secure a relatively long-term loan which permits pre-payments. This assures moderate monthly payments and allows you to pay faster if your earnings permit. If you pay off the loan as quickly as possible, you will save interest costs; you will also build up your equity in the property faster.

Property Taxes

Tax rates on real property vary in different localities. Find out your rates from your local officials or a lending agency. Assessments for civic improvements may be added to your tax bill. Taxes tend to increase over the years.

Insurance

To protect their mortgage loan on the investment, lending agencies require you to carry fire, wind and other insurance on your property. Your policy should also provide enough insurance to protect your equity. See your insurance agent for detailed information.

Upkeep

On new homes, maintenance costs will be small for the first few years, but they will become greater as the house grows older. Over a period of years, you will probably also want to install improved equipment and new conveniences which appear on the market. If you buy an older house, you should allow a greater sum for upkeep than that needed for a new home.

Annual Outlay for Home Ownership on Each $1,000 Borrowed

The table below shows the major expenditures in financing a home after the down payment and preliminary costs are paid.

The payments on the loan and the interest charges are fixed according to the interest rate and the period of payment. They are based on a systematic loan reduction plan (constant monthly payment plan).

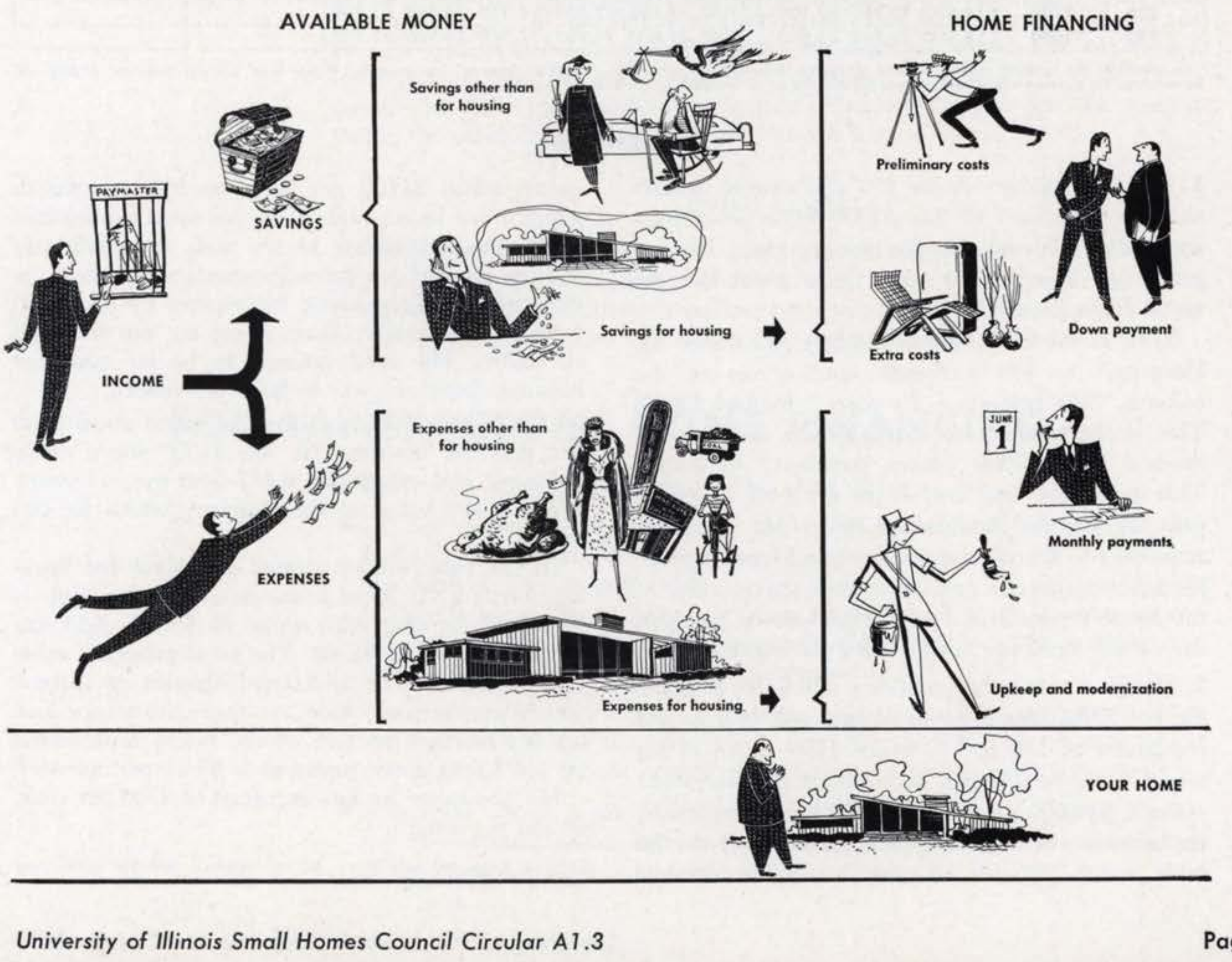
For the purpose of the chart, the expenses **per year for every $1,000 loaned** on the house are assumed to be $18 for taxes and assessments, $3 for insurance, and $20 for upkeep.

Insurance costs will probably be about the same over the years. Taxes and costs of upkeep will vary in different sections of the country. They have been estimated at a reasonable average here because experience has shown that many people do not allow enough for these items. The figures should be adjusted where modifications are known.

	4% INTEREST			5% INTEREST			6% INTEREST		
PAYMENT PERIOD	10 Years	15 Years	20 Years	10 Years	15 Years	20 Years	10 Years	15 Years	20 Years
Interest and Payment on Each $1,000 of Loan per Year* (based on a systematic loan reduction plan)	$122	$89	$73	$127	$95	$79	$133	$101	$86
Taxes and Assessments	18	18	18	18	18	18	18	18	18
Insurance	3	3	3	3	3	3	3	3	3
Upkeep	20	20	20	20	20	20	20	20	20
Total Annual Outlay on Each $1,000 Borrowed	**$163**	**$130**	**$114**	**$168**	**$136**	**$120**	**$174**	**$142**	**$127**

* To find the total payment on interest and principal to maturity for each $1,000 of loan, multiply the annual payment by the number of years in the payment period. Subtract the $1,000 principal from the total payment to find the total interest to maturity for each $1,000 of loan.

Budget Allowance Leading to Home Ownership



HOW EXPENSIVE A HOME CAN YOU AFFORD?

Having determined your budget allowance for housing and the annual cost of home ownership for each $1,000 of the loan, you can now estimate the total amount which you can spend for a home.

The chart below shows the total price of the house that your monthly budget allowance for housing will finance (principal, interest, taxes, insurance and upkeep) at the different interest rates and the different years of payment. It is based on the chart, "Annual Outlay for Home Ownership," on page 5.

To use the table, find your own "Budget Allowance for Housing" in either the monthly or the annual column below. Then read across to the rate of interest which you can obtain and the number of years the loan will run. This figure will give you the amount of the mortgage loan which your budget can finance. Add the amount of the down payment which you can make, and you will have **an estimate of the total cost of the home you can afford.** (The amount of the loan which you can obtain may be much less.)

Remember you must pay taxes, insurance and upkeep on the total value of the house, including both the mortgage amount and your down payment. The table below includes the taxes, insurance and upkeep on the mortgage amount only.

For each $1,000 down payment you will have to set aside approximately $3.50 a month for taxes, insurance and upkeep. (See page 5.) The taxes and insurance can be added to your payments if the lending agency wishes to include these two items in the payments. (The upkeep will be an added expense.)

BUDGET ALLOWANCE FOR HOUSING (from page 3)*		AMOUNT OF MORTGAGE WHICH BUDGET WILL FINANCE									DOWN PAYMENT (Fill in)	TOTAL AMOUNT YOU CAN SPEND FOR A HOME
		4% Interest			5% Interest			6% Interest				
Monthly	Annual	10 Years	15 Years	20 Years	10 Years	15 Years	20 Years	10 Years	15 Years	20 Years		
$25	$300	$1840	$2310	$2630	$1790	$2210	$2500	$1720	$2110	$2360		
30	360	2210	2770	3160	2140	2650	3000	2070	2540	2830		
35	420	2580	3230	3680	2500	3090	3500	2410	2960	3310		
40	480	2940	3690	4210	2860	3530	4000	2760	3380	3780		
50	600	3680	4620	5260	3570	4410	5000	3450	4230	4720		
60	720	4420	5540	6320	4290	5290	6000	4140	5070	5670		
80	960	5890	7380	8420	5710	7060	8000	5520	6760	7560		
100	1200	7360	9230	10,530	7140	8820	10,000	6700	8450	9450		
125	1500	9200	11,540	13,160	8930	11,030	12,500	8620	10,560	11,810		
150	1800	11,025	13,520	15,400	10,620	13,200	14,970	10,230	12,590	14,150		
175	2100	12,860	15,775	17,970	12,390	15,400	17,460	11,940	14,690	16,510		
200	2400	14,700	18,030	20,530	14,160	17,600	19,960	13,650	16,790	18,870		
225	2700	16,530	20,280	23,100	15,930	19,800	22,450	15,350	18,890	21,230		
250	3000	18,370	22,540	25,670	17,700	22,000	24,950	17,060	20,980	23,590		

* In selecting the amount of your budget allowance for housing, remember modifying factors. For example, if less than $20 per year per $1,000 will be required for upkeep, the difference may be treated as an increase in the amount available for housing.

Examples

1. Mr. W's budget shows $50 per month "allowance for housing." He has $2000 for a down payment after allowing for preliminary costs. He can get a 5% loan for 20 years. How much can he spend for a home?

Read down the column, "Budget Allowance for Housing," to $50 a month, and across to the column, "5% interest — 20 years," to find $5000. This is the amount of mortgage his income will finance. Add $2000 (down payment) to $5000. This makes the total cost of the property which he can pay for and maintain $7000. (Mr. W. must remember to set aside approximately $7 per month* for taxes, insurance and upkeep on that portion of the house represented by his $2000 down payment since these items are not included elsewhere.)

2. Mr. H. wants to buy property selling for $10,000. He has $3300 down payment and will borrow the remainder at 5% for 10 years. How much of his income must be set aside to cover cost of ownership?

From $10,000 subtract $3300. This leaves $6700, the amount of loan required. According to the table under "5% for 10 years," a $6760 loan requires about $1100 per year, or $90 per month which must be set aside from his total net income.

He must remember to set aside approximately $12 per month* for taxes, insurance and upkeep on that portion of the house represented by his $3300 down payment since these items are not included elsewhere. The total amount to be set aside for housing, therefore, will be $102 per month.

3. Mr. S. thinks he can afford to spend about $720 per year for housing. He has $1500 for a down payment, and can obtain a 6% loan over 15 years. What is the value of the property which he can afford?

In the table, under annual allowance for housing, locate $720. Read across to column for "6% — 15 years" to find loan value of $5070. Add the down payment of $1500. The total property value thus is $6570. The additional amount of income which must be set aside for taxes, insurance and upkeep on that portion of the house represented by his $1500 down payment is $5.25 per month.*

His allowance for housing must be $780 per year, or $65 per month.

* $18 for taxes and assessments, $3 for insurance, and $20 upkeep per year per $1000 of loan, or approximately $3.50 each month

OTHER EXPENSES—PRELIMINARY, EXTRA

Preliminary costs must be budgeted.

Preliminary Costs

Certain expenses which are "preliminary" to the loan must be budgeted before the size of the down payment can be determined. These expenses vary, depending on whether you are buying or building a home. Some of them may be included in the loan; others must be paid in cash at the time the loan is made. Occasionally some of these expenses are paid by the seller of the property.

When buying a home, preliminary costs usually include:

Appraisal fees.

Loan fees, if any, of your lending agency.

Revenue stamps, notary fees.

Fees for recording the mortgage and the deed to the property.

Legal charges for examining and transferring the title to the property (to show clear ownership).

Pro rata insurance and property taxes (that portion of the taxes and insurance already paid by the seller for which you must reimburse him).

Engineer's survey of property, if needed to establish property lines.

When building a home, preliminary costs include most of those for buying a house, plus such costs as:

Cost of plans or architectural services.

Interest on the loan advances ("pay-outs") to contractors.

Premiums for insurance (fire, theft, hazard and liability, depending on your agreement with your contractor).

Inspection fees.

In "FHA loans," there are usually certain additional preliminary expenses, such as: 1) the first year's mortgage insurance premium; 2) an advance payment for first year's taxes; 3) the first year's premium on hazard insurance; 4) fees for photographs of the house; and 5) FHA loan examination fee. The examination fee is paid when application for the loan is made; the other items must be paid when the loan is closed.

Extra Costs

In building or buying a home, you may find it necessary to incur certain other expenses, such as landscaping, laundry and kitchen equipment (or repair or modernization if an existing house has been purchased). These expenses must be paid for from your savings unless they are included in the loan.

FOR SATISFACTORY HOME FINANCING

- Borrow as little as necessary, instead of as much as you can.
- Do not overbuild or overbuy. If you spend more for housing than your budget will support, you may have to forego necessities as well as comforts. You may even be obliged to sell your property at a loss — or you may lose it. It may be desirable to have a lending agency check your estimate of the amount you can spend for housing, and also advise you on financing the home before you sign any agreement or contract.
- Remember a loan on a home is a serious obligation. It is up to you to tailor your expenditures so that they are in line with the financing charges which you assume. You should expect some changes in income over the years.
- Seek legal advice if you have any doubts about any phase of home financing or ownership — *i.e.,* legality of the title, conditions of the loan, the terms of the general contract, the agreement on occupancy.

OBTAINING THE LOAN

A house should hold up for the life of the loan — and longer.

A mortgage loan on a house entails a risk to both the lending agency which advances the money, and to the prospective homeowner who promises a large part of his income for a period of years in payment for the house.

In return for its risk, the lending agency has a legal claim to the house for security until the loan is repaid; the homeowner, on the other hand, has the use of the house and the promise of eventually owning it free of debt. Both the lending agency and the homeowner therefore are interested in the house until the loan is paid in full.

Because of the long-time investment involved, the house, to be a good risk for both the homeowner and the lending agency, must be so located, designed, and constructed that it will retain a value well in excess of the loan balance for not only the period of the loan, but longer. The risk of depreciation (or depression in the value) of the property must be assumed by the homeowner.

Home financing is a mutual program as far as the homeowner and the lender are concerned. To avoid loss to either or both, the home must be financed on a sound basis. A sound mortgage is one in which 1) the prospective homeowner's credit record indicates that he will be able to make the loan payments; and 2) if unforeseen events occur which prevent the homeowner from making his payments, the value of the house at that time will be sufficient to satisfy the unpaid balance of the loan (the mortgage debt).

A foreclosure is not desired by either the lending agency or the homeowner.

The Lending Agency

The lending agency's "stock in trade" is money — not property. Its funds usually represent savings of individuals for which the lending agency is acting as a trustee. These savings must be protected. The lending agency, therefore, does not want to take over property any more than the homeowner wants to lose it. The agency wants only to receive interest on its money while it is being used and to have the money returned.

The Homeowner

To obtain a loan, the prospective homeowner must establish himself as an approved credit risk. He must assure the lending agency that his income (earning capacity) and his reputation for paying debts warrant a loan being made to him. His credit record also is an important consideration in determining the amount of the loan which can be made.

In obtaining any loan, the homeowner should make a point of understanding thoroughly every detail — *i.e.,* how much he must pay, when he must pay it, and exactly what property he is pledging as security. He must recognize as a serious responsibility his obligation to pay back the cash he is borrowing.

Home financing is a mutual program for borrower and lender.

Federal Credit Regulations

All lenders operate under certain governmental regulations. Before you incur any financial obligations related to your home, ask your lending agency about current governmental regulations that tend to either liberalize or restrict home financing.

TYPES OF MORTGAGE LOANS

Mortgage loans are classified by the plan for repaying the loan. There are several types, but the one most commonly used today is the **constant payment plan** (the regular amortized mortgage loan).

Under this systematic loan reduction plan, the homeowner at regular intervals (usually each month) pays a fixed amount which includes both interest and payment on the loan principal. The monthly payment is the same during the life of the loan. That part of the monthly payment which is used to repay the loan principal increases each month since the amount paid for interest decreases. (Interest payments become less as the loan principal becomes less.)

For example: A homeowner borrows \$8,000 at 5% interest on a 15-year loan. His monthly payments are \$63.27 for a period of 15 years. The interest the first month on the \$8,000 will be \$33.33. The payments on the principal will thus be \$29.94, making the unpaid balance, \$7,970.06. The interest in the second month will be 1/12 of 5% on the \$7,970.06 or \$33.20. This leaves \$30.07 to be paid on the loan principal, making the unpaid balance \$7,939.99. In this manner, payments continue to reduce the loan so that at the end of 15 years the loan is repaid.

Monthly payments are the most popular.

Taxes and property insurance premiums may be included in the regular monthly payment. These are in addition to the interest and loan payments. If taxes should increase, these monthly payments would increase.

A variation of the regular amortized mortgage plan is the open-end plan. A clause in the mortgage gives the borrower the privilege of obtaining additional funds (for purposes such as remodeling) after the loan has been reduced without going through the formality of rewriting the mortgage. The total loan outstanding at any time is usually restricted to the amount of the original loan.

Other amortized mortgage plans permit increasing payments or decreasing payments each month. These are not in common use.

Another type of mortgage is the straight mortgage. It is used less today than formerly. This plan requires that the loan be paid in full on a specified date (usually one to five years). Interest is paid at stated periods. (The terms of the loan may permit pre-payment.)

FHA and VA Loans

Frequent reference is made to "FHA loans" and "GI or VA loans." These are not mortgage plans, but are government insurance or guarantees on loans. The government does not provide the money for the loans; the funds come from the lending agencies through which homeowners obtain loans. The government merely sets up credit and building standards which, if met, permit the loan to be insured by the FHA (Federal Housing Administration) or guaranteed in part by the VA (Veterans Administration).

FHA borrowers underwrite the insurance since each pays ½ of 1% of the amount outstanding on his loan into a common insurance pool each year. This pool covers any loss and may pay dividends to the borrowers if losses are small. This FHA insurance premium is included in the borrower's monthly payments. GI borrowers pay no insurance fee on VA guaranteed loans.

The insurance and guarantee features of FHA and VA loans liberalize home financing since they protect lenders against loss, thereby reducing the large margins of security which lending agencies set up to protect themselves. Lenders thus are induced to make larger loans in relation to the value of a house than they could without the guarantee. Since most lenders are trustees for other people's savings, either a safe margin of security or government assurance against loss is necessary.

FHA borrowers pay ½ of 1% of the amount outstanding on their loans into a common insurance pool.

Package Loans

Often when a family buys a newly completed house from a contractor or enters into a contract for the building of a home, the financing has been previously arranged by the contractor who offers a "package" loan. Under it, the buyer pays a regular amount monthly over a period of years. This includes payment on the loan principal, interest, taxes, insurance. If you should assume a "package" loan, make sure you understand its terms.

WHERE TO GO FOR A LOAN

Choose your lender with care.

Every mortgage transaction involves individual problems of financing. Seek advice about loans from reliable lending agencies before you obligate yourself in any way. Established sources of loans (listed alphabetically) include:

- Banks (commercial and savings).
- Mortgage bankers who represent individuals, banks, insurance companies or other institutional investors.
- Savings and loan associations (or building and loan associations).
- Title and trust companies who may loan their own funds.

Having decided on home ownership and a specific piece of property (either an existing house, or land on which to build a house), you should consult one or more reliable lending agencies in your community about a possible loan. Explain your problem, investigate their terms, ask questions, and talk the matter through in detail. Remember that lending agencies are in competition with each other just as any other business firm. Try to find the agency that will give you the type of loan that best meets your requirements.

Information Needed

To evaluate the loan plans offered by various lending agencies you must have certain information. Ask the agencies questions such as:

- **How soon can I get the loan?** (FHA and VA loans may take longer than others.)
- **What are the terms of the loan?** What are the interest rates? How many years will the loan run? Can this period be extended at a later date? Approximately what will be the total amount of interest? What is the amount of monthly payments? Is there a period of grace? Is there a penalty for failure to pay on time?
- **What method of paying taxes do you require?** Do I pay my own taxes? Can tax money be included in the monthly payments?
- **Is a monthly deposit of funds required to pay insurance?** What kind of insurance must I carry? How much?
- **Are there pre-payment privileges?** If so, on what basis can I make payments in advance of the amount due as stated in the loan contract? Is there any penalty for advance payments? Can I pay off the loan in full prior to its maturity? Will pre-payments be credited as regular payments at a future time if I wish this? In case of pre-payments, will I pay interest only on the balance due?
- **When are the payments due?** Do I receive notification of due date?
- **What "preliminary" costs will I have?** What will they amount to? When do they have to be paid? Can they be included in the loan?
- **Can my "extra" costs be included in the loan?**

Construction Loans

Builder frequently must be paid as he completes various stages of work.

If you are going to build a house, you will probably need money to pay your builder as construction progresses. If so, ask lending agencies whether you can get money for these advance pay-outs to your builder. Find out the charges for such a construction loan. Ask:

- **At what stages of the construction can I get the money?** Can I arrange these construction loan advances and my final mortgage as one contract? Who will handle the entire payments to the builder (my funds as well as those loaned to me)?
- **What inspection, if any, is provided as a check that my house will be built according to specifications?** Or, is it my responsibility to have inspections made by an architect or other qualified person?

Consult a lending agency on the **possibility** of obtaining a loan before you incur large expenses for plans, working drawings and specifications. Later, when the possibility of getting a loan is assured, you will need plans and specifications so that the amount of the loan can be determined.

APPLYING FOR A LOAN

Having found a loan plan which meets your needs, you are now ready to make application for a loan. This is your formal request for the loan from the lending agency which you have selected.

Application

Application

Information generally asked for in application forms includes:

- The amount of loan you want.
- The terms and conditions of the loan requested (including whether a GI or FHA loan is desired).
- Personal data so that the lending agency may judge your credit responsibility. This information will include credit references, current income, current obligations, possible future expenses.
- Identification and description of the property on which you want the loan and which you will pledge as security.

Investigation

On the basis of the application form, the lending agency will verify: 1) the personal information submitted, 2) the fact that you have — or will have — the property described, and 3) your right to pledge the property as security.

Property Appraisal

The lending agency before granting the loan must form an opinion as to the value of the property described. This is a point which can present misunderstandings since the borrower's appraisal and the appraisal of the lending agency may not agree. For this reason, the latter's valuation is generally not revealed to the borrower.

Investigation

The lending agency's appraisal is not on a man's house as property on the current market, but as security. It represents the market value of the property during the life of the loan if the house should ever be sold. It does not recognize the high prices of homes in inflationary periods, nor does it recognize special usefulness to a particular homeowner. The property might cost a great deal and be very desirable to one family, but it might not have an appeal to other people should it be offered for sale. (In a GI loan transaction, the price of the property cannot exceed the VA appraisal.)

Factors which determine the desirability of the property over a period of time and, as a result, the lending agency's appraisal are:

- The location as regards community and neighborhood. (Before buying a lot, check the suitability of location with a lending agency.)
- Size of property (both lot and house).
- Physical soundness of the structure.
- Desirability of the architectural design of the house.

If a construction loan is desired, these points are judged by plans, working drawings and specifications.

Decision as to the Amount of the Loan

After investigating your credit rating and appraising the property to be financed, the lending agency tells you how much it can lend.

If you cannot obtain the amount of the loan you need from the first lending agency you interview, try another reliable agency. If this application does not result in the desired loan, re-examine your proposal to see what is wrong with it. It may be that your house is too individual in its design, or the site you have tentatively selected is poorly located, or your earning capacity is not great enough to carry the amount of the loan you need.

In an FHA loan, the appraisal of the Federal Housing Administration determines the amount of the loan which it will insure.

Appraisal

Letter of Commitment

Usually, before the loan is formally granted, the lending agency will issue a letter of commitment in which the terms of the mortgage are outlined. This enables you to make contracts with an architect and contractors, and also to proceed with arrangements to purchase property. Be careful about making any payments until your lending agency has definitely committed itself to granting the loan.

CLOSING THE LOAN

After the loan has been approved, title records of the property must be examined. Certain papers must be signed in order to "close the loan." At that time: 1) you are usually required to make your down payment (or to pay the rest of it if you have already paid part) and to pay the preliminary costs; and 2) funds are turned over to you by the lending agency so that you can complete your purchase. Documents you will sign are:

- **The note or bond** — The promise to repay the money borrowed.
- **The mortgage** — The pledge of property to secure your promise that you will repay the principal and also pay the interest.
- **Affidavits and receipts** relating to the above two documents.

In these papers, you will be referred to as the mortgagor; the lending agency as the mortgagee. Before signing any of these documents, you should read them carefully, making sure that you understand them thoroughly. If you do not, ask questions or consult your attorney. Documents usually involved in the closing of a loan are described in the chart below.

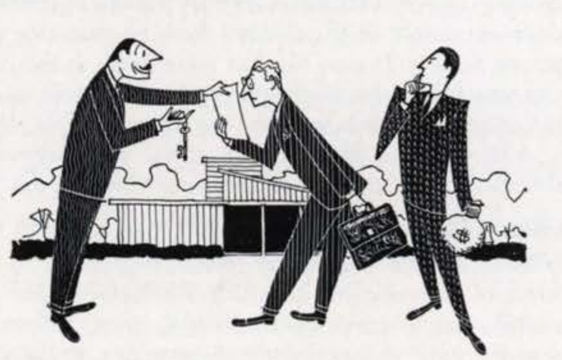
DOCUMENTS	PURPOSE	PROVISIONS	HOLDER	REMARKS
Note or Bond	The promise to repay the money borrowed.	Sets forth: • Amount of loan. • Conditions of the promise to repay.	Lending agency until loan is repaid.	You should have a copy.
Mortgage	Pledge of property to secure the promise to repay.	• Sets forth conditions under which you pledge the property as security. • Gives lender the power to acquire the property if you fail to repay the loan as agreed.	Lending agency until loan is repaid in full. That the loan has been discharged is then entered on the public records.	You should have a copy.
Deed* (to the property)	Evidence of ownership.	Presents evidence that you own the property.	In some states, the deed with revenue stamps on it is recorded and given to you; in others, it may be held in trust by a third party (in escrow) until the loan is repaid.	• Deed should be recorded by county register-of-deeds. • You should have either the deed or a copy of it.
Certificate of Title* (or Opinion of Title)†	Assurance that title to property is unmistakably in your name.	Declares that the title to the property is "clear" or "marketable"—that is, no one else has claim to the property except you. (It is derived from the abstract.)	You, the homeowner. (This is usually given you with the deed.)	• Be sure the title is investigated. • Title search is usually arranged for by lending agency. Certificate is prepared by an attorney or by a title company.
Abstract†	Legal description of property and history of previous ownerships.	Describes property and all transactions back to grant from United States government. (It is prepared by an abstract company and checked by an attorney.)	Lending agency until loan is paid in full.	• If you have a certificate of title, you probably will not get the abstract. • The abstract should have the deed and mortgage recorded on it.
Fire Insurance Policy	For protection of loan on property and your equity.	Is written in your name with a mortgagee clause attached.	Lending agency.	• You should have a copy. • Be sure amount of insurance is sufficient to protect your equity.

* Where the Torrens system is used, deed and title procedures differ.
† Title insurance may be advisable. For one premium, your claim to ownership is protected as long as you own the property.

ASSUMING AN EXISTING MORTGAGE

If you are considering the purchase of a house with an existing mortgage, be certain that you understand the terms of the loan as previously made, as well as the terms of the purchase contract. Weigh these terms against your budget allowance for housing to make sure that you are financially able to handle the obligations.

In assuming such existing indebtedness, have the papers examined by someone who is qualified to advise you. Be particularly cautious on the matter of **when** actual ownership is conveyed to you. As evidence that you have paid your money and own the property, you should possess the deed and the opinion of clear title.



Have the papers examined by someone who is qualified to advise you.